



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: 201002042
Release Date: 1/15/2010

Date: October 20, 2009

UIL: 501.12-02

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

State =

Dear :

We have considered your letter of December 29, 2008, requesting a ruling on the proposed transaction described below and its tax consequences on your federal income tax exemption under Section 501(c)(12) of the Internal Revenue Code.

FACTS

You are organized as a not-for-profit corporation under the laws of State for the purpose of installing and maintaining a telephone system, exchange, and lines for the mutual benefit of your members. In addition, your bylaws allow you to furnish electricity, natural gas, and water to your members on a cooperative basis. You represent that you are a cooperative as described in section 501(c)(12) of the Code.

You are currently building substation communication infrastructure for purposes of implementing Supervisory Control and Data Acquisition (SCADA) capability. You indicated that SCADA is the first major step for ultimately achieving two-way data communications with individual member households and businesses. The purpose of the SCADA system is for remote monitoring and control of assets in electrical substations and power line protection. The monitoring function of SCADA includes retrieving real-time load data, switch status, and equipment failure alarms. You also indicated that once constructed and operational, the SCADA infrastructure can also serve as the backbone for providing broadband high-speed "telecommunications/broadband services" (i.e., Internet) coverage and e-mail service to members throughout your service territory and perhaps beyond.

RULINGS REQUESTED

Your furnishing of wireless high-speed telecommunications/broadband service to your members is consistent with section 501(c)(12)(A) of the Code, provided you continue to meet the statutory requirements for exemption.

LAW

Section 501(c)(12) of the Code provides for the exemption from federal income tax of benevolent life insurance associations of a purely local character, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations; but only if 85 percent or more of the income consists of amounts collected from members for the sole purpose of meeting losses and expenses.

Rev. Rul. 72-36, 1972-1 C.B. 151, describes certain requirements that cooperative companies must meet to be exempt under section 501(c)(12) of the Code. Those include the requirement that the rights and interests of the members in the savings of the organization be determined in proportion to their business with the organization. The interests of members in the savings of the organization may be determined in proportion to either the value or the quantity of the services purchased from the organization. To maintain its mutual or cooperative character, an organization must keep such records as are necessary to determine, at any time, each member's rights and interests in the assets of the organization.

Rev. Rul. 57-420 held that a nonprofit organization which provides and maintains a two-way radio system for its members on a mutual or cooperative basis qualifies for exemption from federal income tax under section 501(c)(12) of the Code as a "like organization," provided 85 percent or more of its income consists of amounts collected from members for the sole purpose of meeting losses and expenses.

In Puget Sound Plywood v. Commissioner, 44 T.C. 305 (1965), acq. 1966-1 C.B. 3, the court held that an organization must meet certain common law requirements in order to be a cooperative. These common law requirements include: democratic control of the organization by members, the organization operates at cost for the benefit of members, and the contributors of capital to the organization do not control or receive most of the pecuniary benefits of the organization's operations (i.e. subordination of capital).

ANALYSIS

Organizations exempt under section 501(c)(12) include entities providing and maintaining two-way communication services to their members. In Rev. Rul. 57-240, the Service concludes that an organization that provides and maintains a two-way radio system is a "like organization" for purposes of section 501(c)(12) because it has a purpose similar to that of a mutual telephone company, allowing members and patrons to communicate with other people. In the situation here, the high-speed telecommunications/broadband services via SCADA system technology will allow your members to communicate with others, sending and receiving messages through this technology. It serves the same purpose for which the organization described in Rev. Rul. 57-240 was held to be exempt under section 501(c)(12) of the Code. Hence, this service is an activity described within the meaning of section 501(c)(12)(A).

Exemption under section 501(c)(12) also requires a cooperative to satisfy the 85 percent member income test. In calculating the 85 percent member income test, a cooperative must combine income derived from all sources to calculate whether 85 percent of its income is derived from members. See section 501(c)(12)(A) of the Code. Hence, in each taxable year you must combine income derived from the provision of all services, including broadband communications, telephone, electricity, natural gas, and other sources to determine whether you satisfy the 85 percent member income test.

Rev. Rul. 72-36, *supra*, describes additional requirements that are fundamental to the organization. Namely, a cooperative must keep adequate records of each member's rights and interests in the assets of the organization. A cooperative must not retain more funds than it needs to meet current losses and expenses. The rights and interests of members in the organization's savings must be determined in proportion to their business with the organization. In keeping with Rev. Rul. 72-36, you account on a patronage basis to your patrons for all amounts received and receivable from the furnishing of these services in excess of operating costs and expenses.

Your operations must also meet the requirements stated in Puget Sound, namely: democratic control by the members whereby member are entitled to only one membership and one vote. You will operate at cost. Furthermore, patrons' equity accounts will consist of allocated, but unredeemed net savings from the cooperative's telecommunications and other "like organization" operations.

Therefore, as long as your telecommunications/broadband services are conducted on a cooperative basis, and 85 percent or more of your income is from members and used solely for meeting your losses and expenses, your provision of this service is consistent with the established requirements under section 501(c)(12) of the Code.

Accordingly, we hold as follows:

Your furnishing of wireless high-speed telecommunications/broadband service to your members is consistent with section 501(c)(12)(A) of the Code, provided you continue to meet the statutory requirements for exemption.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. A copy of this letter should be kept in your permanent records.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, Notice of Intention to Disclose. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Theodore R. Lieber
Acting Manager, Exempt Organizations
Technical Group 3

Enclosure
Notice 437